

STATEMENT OF
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UNDER SECRETARY OF DEFENSE
(PERSONNEL AND READINESS)

Before The
Personnel Subcommittee
Senate Armed Services Committee

ON
Military Pay and Retirement

March 3, 1999

Mr. Chairman and members of the Subcommittee, I am pleased to appear today to discuss military pay and retirement, the two areas that form the foundation of the military compensation system.

The Department of Defense is proposing three primary initiatives to improve pay and retirement programs for the men and women of our armed Services. These initiatives are designed to more fairly compensate military members for their outstanding performance and dedicated service to our nation. Specifically, the Department's pay and retirement budget request for fiscal year 2000 includes: Across-the-board pay increases for all service members, targeted raises that provide greater reward for performance, and improvements to the military retirement program that provide greater equity among career service members. I would like to highlight each of the proposals and discuss them in greater detail.

The Department of Defense today faces multiple force management challenges: our country's strong economy offers tremendous job opportunities to our highly trained military members; individuals affected by the Military Retirement Reform Act of 1986 are reaching key decision points in their career; and the current tempo of deployments is causing many members and their families to think twice about the demands and lifestyle of a full career in the military. The President recognizes the extraordinary efforts of the men and women serving in the Armed Forces today and has submitted a fiscal year 2000 budget that responds to those challenges with a fully funded program of pay and retirement improvements. The major components of the fiscal year 2000 "compensation triad" include:

- **Across-the-board pay increases for all service members:** Effective January 1, 2000, all service members would receive a raise of 4.4 percent -- the largest increase in basic military pay in nearly a generation. In addition, annual raises matching the currently forecasted rate of civilian wage growth have been programmed in fiscal years 2001 through 2005. These pay raises would ensure our service members continue to be compensated adequately and fairly.

- **Targeted raises and greater reward for performance:** In addition to across-the-board pay increases, non-commissioned officers and mid-grade commissioned officers would receive additional raises. These proposed adjustments would better reward performance by compensating military personnel for the skills, education, and experience they have acquired and would provide greater incentives to continue military service. These changes would also result in the first systematic reform of the military pay table in nearly 50 years.
- **Improving the military retirement system to meet changing times:** The retirement system that applies to service members who entered after 1986 has increasingly become a source of dissatisfaction and internal inequity. The proposal would restore 20-year retirement to 50 percent of basic pay, and would provide for modest changes to the annual Cost of Living Adjustment for retiree pay.

WHY IT IS IMPORTANT TO ACT NOW

America's Armed Forces are operating under a combination of influences never before encountered. The end of the Cold War fundamentally changed the demands placed on America's military. A single, global adversary has given way to multiple global demands on U.S. forces that are no longer forward-deployed. At home, the nation is experiencing economic prosperity and a growing demand for advanced technological skills and knowledge. These economic developments, welcome as they are, have created sharper competition for the high quality men and women needed in America's Armed Forces.

The expertise and leadership for which America's Armed Forces are renowned is developed through years of training and experience. We need to preserve that expertise and leadership because it takes years to regain if lost. The Department's proposal recognizes this, and works to prevent the loss of our critical mid-grade personnel. Our mid-grade personnel not only provide the leadership that makes today's force the most capable in our history but they also serve as teachers and mentors to our more junior grade members who eventually will succeed them. Consequently, we propose not only to raise pay across the board for all service members, but also

to institute pay table reform that would compensate mid-grade service members for their outstanding performance. We believe that these proposals, coupled with our retirement proposal, will maintain the high quality of personnel recruited and retained in America's force well into the 21st century.

THE COMPENSATION TRIAD

ACROSS-THE-BOARD PAY INCREASES

Pay raises send a clear signal that our nation recognizes the demands and sacrifices of military service. The military pay raise would ensure that service member pay remains at least slightly ahead of private sector wage growth. It would also assure that entry level pay could continue to attract high quality recruits given a wide array of civilian workforce and education alternatives. The proposed 4.4 percent across-the-board raise costs \$850 million in fiscal year 2000 and has a total cost of \$14 billion, with an additional \$10 billion for the department's civilian employees, over fiscal years 2000 through 2005.

TARGETED RAISES AND GREATER REWARD FOR PERFORMANCE

Basic pay is the most fundamental and visible element of a military member's compensation. In addition to the across-the-board raise in basic pay, the Department of Defense proposes changes beginning July 1, 2000, to provide targeted pay increases for non-commissioned officers and for mid-grade commissioned officers. These raises are targeted at the grades where experience, skills and knowledge are most valuable to the Services and to the larger civilian economy. The maximum targeted pay increases would range up to 5.5 percent and would come on top of the 4.4 percent that all military personnel would receive beginning January 1, 2000. This proposal cost an additional \$190 million in fiscal year 2000 with a total cost over fiscal years 2000-2005 of \$4.5 billion.

Previous changes to the military pay table have had the effect of weighting longevity more heavily than promotion for pay increases. Our proposal provides service members with

progressively higher pay increases for each promotion they receive. The pay increases for promotion will generally be greater than those tied to longevity, and longevity increases will become more uniform over the course of a military career. Placing greater emphasis on promotion pay better recognizes career non-commissioned officers and commissioned officers for their performance.

This proposal -- the first systematic change to the pay table in nearly 50 years -- was based on studies conducted during the 7th Quadrennial Review of Military Compensation (QRMC), validated by the 8th QRMC, and vetted by the Services.

RETIREMENT

The military retirement system is unique among federal and private sector systems because it reflects the unique demands and limitations placed on its recipients during their careers. Military members serve at risk of life and limb, routinely suffer long and difficult family separations, and endure frequent, mandatory moves to meet the requirements of their respective Services. Because the armed Services must be combat-ready, they must be staffed with young and physically vigorous men and women. This requires most career members leave military service in their 40s – a time in life when they would be entering their peak earning years had they made another career choice. Military retirement at 50 percent of basic pay is equivalent to approximately one-third of total pay and allowances. This amount represents both deferred compensation for the rigors of a military career, as well as compensation for leaving that career early to allow us to maintain a vigorous and ready force.

The Military Retirement Reform Act of 1986, also commonly referred to as REDUX, provides service members who entered service after 1986 with 40 percent of basic pay for retirement at 20 years of service – or approximately one-fourth of their total pay and allowances. REDUX was one of a series of reforms designed during the latter years of the Cold War to support an All Volunteer Force at a time when the force was much larger and had a very different deployment profile. One aim of the 1986 change was to encourage greater retention beyond 20

years of service. In addition to promoting longer retention for some, it was anticipated that it would result in a manageable decrease in retention of service members with 10 to 20 years of service.

When the Military Retirement Reform Act of 1986 was enacted, America's military numbered 2.2 million members. Today, our force numbers 1.4 million, and the loss of service members with 10 to 20 years of service is a growing concern. With the growing technological complexity of today's military, it takes longer to train personnel to reach their full capacity, and the loss of highly-skilled mid-career personnel is felt all the more keenly.

Force management during the Cold War was different than that practiced today. At the time REDUX was enacted, adequate performers in the career force were largely guaranteed that they could serve as much of a 30 year career as they chose. This choice of how long to serve somewhat offset the financial uncertainty service members faced by leaving a career in their prime earning years.

Force management during the drawdown created a new dynamic with the Services using a variety of force shaping tools to control who remained on active duty. An unintended consequence of the drawdown is that there is now much greater uncertainty among military members over whether or not to commit to a career. Service members today not only face greater uncertainty about how long they may be allowed to stay, but also recognize that their 20 year retirement is less valuable than their predecessors. Indicators of service member dissatisfaction are apparent in surveys conducted of separating personnel: dissatisfaction with both pay and retirement has risen in relative importance over the past several years, most notably in year groups subsequent to 1986 when the retirement system was last changed.

The Department's retirement proposal is designed to address these issues and to ensure a high-quality All-Volunteer Force. Restoring the 50 percent multiplier and providing for modest changes to the annual Cost of Living Adjustment for retiree pay will cost \$800 million in fiscal year 2000, and a total of \$6 billion over fiscal years 2000 through 2005.

SPECIAL AND INCENTIVE PAYS

In addition to the triad of pay and retirement initiatives, the Department continues to rely heavily on Special and Incentive pays targeted at the most critical skills. These pays, all of which are fully funded in the President's Budget, will bolster the near and long-term readiness of our Armed Forces. In concert with proposed pay and retirement improvements for all members, the employment of such targeted pays for specific skills is cost effective and is expected to substantially improve the Department's ability to attract and retain top people.

RETENTION

The retention climate among all Services has become more challenging. Our nation is experiencing the strongest economy in the history of the All-Volunteer Force. A strong economy, coupled by the tremendous growth in the technology sectors, has opened a range of opportunities in the private sector for our highly-trained men and women in uniform. The self-discipline associated with military duty, the level of responsibility placed on today's members, and the technical training we provide, all serve to make military experience a valuable commodity in the job market. Attractive salary and benefits packages, coupled with greater geographic stability and a more predictable lifestyle, are key influences in the pursuit of private-sector opportunities.

Let me turn to a few of the indicators that show a pressing need for the compensation improvements we are proposing for fiscal year 2000.

OVERALL RETENTION

The Army met overall enlisted retention goals for fiscal year 1998 and remains generally on course for fiscal year 1999. Looking at retention in the aggregate, however, masks significant shortfalls in specific skills. Addressing retention has proven difficult and expensive in all areas. The Army increased its overall retention mission by nearly 3,000 between FYs 1998 and 1999,

which relieved pressure on recruiting efforts; however, to achieve that goal, the Army was compelled to boost its Selective Reenlistment Bonus (SRB) budget by \$24 million.

The Navy missed its enlisted retention goal for fiscal year 1998, and remains below goal this year. The number of sailors opting for short-term extensions rather than longer-term reenlistments has risen steadily since fiscal year 1996.

The Marine Corps met fiscal year 1998 retention goals, and has accomplished 65 percent of its annual mission to date. The Corps does not foresee significant difficulties in meeting fiscal year 1999 targets, but is closely watching career fields with troublesome loss patterns in signal intelligence, data processing, and avionics.

First-term retention in the Air Force dropped 10 percent during the first quarter of fiscal year 1999. The Air Force has more than doubled SRB funding since fiscal year 1995 and is now offering SRBs totaling \$53 million to more than 100 career fields.

PILOT RETENTION

The retention of pilots continues to present a major concern for the Department, particularly in the Navy and the Air Force. *Air Incorporated*, an independent agency that projects commercial airline hiring for the 14 major airlines, projects a requirement for 18,000 new airline pilots through fiscal year 2004.

The dilemma for Air Force pilot manning is that for every two pilots who enter the Air Force, three are currently leaving. At this pace, the Air Force expects to be short at least 2,000 pilots by fiscal year 2002. In the Navy, current shortages are limiting the flow of aviators to vital Department Head billets. This will require officers in those billets to extend sea duty tours -- already running 7 to 9 months beyond the 36 month standard -- to even longer periods. Keeping pilots at sea longer is likely to have a negative effect on retention. The Marine Corps is currently able to meet its aviator requirements, but is closely monitoring a recent decline in the bonus take

rate among the fighter/attack and electronic warfare communities, a leading indicator of pilot retention behavior. Fixed wing pilot take rates in those specialties for fiscal year 1998 were about half of the fiscal year 1997 rate. The Army's greatest aviation challenge centers on warrant officers who pilot the Apache helicopter. The Army began fiscal year 1999 with 925 pilots against a requirement for 1,059. To respond to that challenge, the Army began offering a pilot bonus for the first time in its history.

OTHER RETENTION CONCERNS

While pilot retention remains a critical concern, other career fields present challenges as well. Since 1993, the Navy's Surface Warfare Officer (SWO) Community has fallen short of its required retention rate. This has forced an extension of sea duty for an additional 8 to 10 months. The Army is also reporting growing concern over an unexpectedly high loss rate for captains, who -- at 35 percent of its officer corps -- are essential to unit performance. A survey conducted by the Army Research Institute (ARI) suggests that these losses are attributable to perceived losses in pay and retirement, greater deployment tempo, and excellent private-sector opportunities.

The pay and retirement initiatives contained in the President's fiscal year 2000 budget are intended to help reverse these negative trends. The retention effects of the three-part improvement to military compensation were modeled by the RAND Corporation based on retention patterns within the enlisted force. A combined package including a 4.4 percent overall pay raise, targeted pay raises, and an increase in the retired pay multiplier from 40 to 50 percent at 20 years is estimated to increase retention rates by 6 percent at the first reenlistment point and 13 percent at the second reenlistment point, with a 20 percent impact on retention for those members reaching 20 years of service.

The Department recognizes that not all solutions are monetary. In fact, senior leadership continues to focus on segments of the force that may be over-stressed by deployment patterns. The Army has initiated the rotation of stateside units to Bosnia in order to reduce operational strain on units in Germany. Additionally, a Texas National Guard Division has been designated to assume

the Bosnia mission in fiscal year 2001. The ongoing implementation of the Air Force's Expeditionary Aerospace Force (EAF) will help to stabilize deployments; and the Navy's reduced training tempo during the inter-deployment training cycle will ease burdens for members and families between periods of extended deployment.

RECRUITING

fiscal year 1998 was a difficult recruiting year. Although not fully successful in attracting the numbers of new recruits sought, the Services did enlist young people with the education and aptitude levels necessary to sustain a capable, ready force. The Services recruited nearly 180,000 first-time enlistees -- 94 percent were high school diploma graduates (HSDGs) with 68 percent scoring above average on the enlistment test. Through the first four months of this fiscal year, the Navy and Marine Corps met their numeric recruiting goals, while the Army and Air Force fell short at 87 percent and 94 percent, respectively.

The Army has increased recruiting resources by more than \$100 million above its planned fiscal year 1999 investment, including raising the enlistment bonus (EB) ceiling for three-year enlistments from \$4,000 to \$6,000. Both the Army and Navy have implemented a new \$3,000 EB for those enlisting in historically low-flow months (February to May). The Navy is also increasing its recruiter strength by 10 percent (up to 4,500) by March 1999. Moreover, the Air Force has increased its fiscal year 1999 advertising budget from \$16 million to \$39 million and front-loaded \$37 million for fiscal year 2000 advertising. The Air Force also is working to fill an 18-percent deficit in recruiter manning. The Army and Navy have added to their College Fund "kickers" -- additions to Montgomery GI Bill benefits -- to increase their "money-for-college" incentives from \$40,000 to \$50,000.

In fiscal year 1999, the Services found that the combined impact of a robust economy and rising college attendance necessitated higher recruiting budgets in order to be successful. The \$113 million added in the fiscal year 1999 Readiness Supplemental was helpful and sorely needed by the Navy and Marine Corps. The Army added over \$100 million during the year, primarily

toward enlistment incentives. The Air Force also is adding money to its enlistment bonus and advertising programs.

Improvements in compensation also will help stimulate our recruiting efforts. The robust U.S. economy has produced the lowest unemployment rate experienced during the history of the All-Volunteer Force. This economy, coupled with ever-increasing youth college attendance, has created a tremendous challenge for military recruiting. Annual youth attitude surveys indicate that interest in the military (enlistment propensity) has fallen since Operation Desert Storm, although there are recent signs that this decline in propensity has stabilized. As a related matter, the end of the military drawdown, along with growing retention challenges, have increased service accession goals.

Taken together, these factors present serious challenges, both short and long range. We believe that enactment of the compensation triad proposed in the President's fiscal year 2000 budget is an important step in addressing these concerns.

Summary

Nearly every day we are reminded of the benefits that have accrued to our nation -- and to the world -- from our predecessors' decisions to support an All-Volunteer Force. We see the benefits of an All-Volunteer Force in unprecedented economic growth -- a product of a relatively stable world in the wake of our Cold War victory -- and in the extraordinary performance of America's military in Operation Desert Fox, peace-keeping operations in Bosnia, and hurricane recovery operations in Honduras.

We now face mounting challenges to our ability to recruit and retain the quality men and women needed to sustain the success of our All-Volunteer Force. The military pay and retirement initiatives included in the President's Budget are part of a larger effort to meet these challenges that include quality of life enhancements, improved housing and subsistence allowances, and targeted special and incentive pays. These initiatives aim to provide a pay and compensation system that is

both fair and competitive in attracting and retaining the high quality men and women needed to sustain the readiness of America's All-Volunteer Force.

We remain grateful for your unfailing support of those who serve our nation.